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Homeland Security

United States  
Coast Guard



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COMDTNOTE 4121

OCT 4 2006

COMMANDANT NOTICE 4121

CANCELLED: OCT 3 2007

Subj: CH-7 TO THE COAST GUARD UNIFORM SUPPLY OPERATIONS MANUAL,  
COMDTINST M4121.4

1. PURPOSE. To provide changes to the Coast Guard Uniform Supply Operations (USO) Manual, COMDTINST M4121.4.
2. ACTION. Area and district commanders, commanders of maintenance and logistics commands (MLCs), commanding officers of headquarters units, assistant commandants for directorates, Judge Advocate General, and special staff offices at Headquarters shall ensure compliance with the provisions of this Notice. Internet Release Authorized.
3. DIRECTIVES AFFECTED. None.
4. SUMMARY OF CHANGES. This notice reflects policy changes to USO Manual Chapter 16. The policy changes are to correct DHS Inspector General audit findings and update Coast Guard policy and procedures for conducting physical inventories at Aircraft Repair and Supply Center (ARSC) and Engineering Logistics Center (ELC). ARSC and ELC are updating their internal procedures in accordance with these policy changes.
5. PROCEDURES. Remove and insert the following pages:

REMOVE

Chapter 16

INSERT

Chapter 16

6. ENVIRONMENTAL ASPECT AND IMPACT CONSIDERATIONS. Environmental considerations were examined in the development of this notice and have been determined not to be applicable.

DISTRIBUTION – SDL No. 145

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7. FORMS/REPORTS. None.

/s/

D. G. GABEL

Rear Admiral, U.S. Coast Guard

Assistant Commandant for Engineering and Logistics

Encl: (1) CH-7 to Uniform Supply Operations Manual, COMDTINST M4121.4

## CHAPTER 16 - PHYSICAL INVENTORY POLICY AND PROCEDURES

### A. Overview.

1. The physical inventory control program addresses the policy, procedures, accountability and responsibilities the Inventory Control Points (ICPs) have for maintaining:
  - a. Consumable Spares,
  - b. Reparable Spares, and
  - c. Inventory (Supply Fund and YARD Fund).
2. Unless otherwise specified, any reference to “inventory” in this chapter includes Consumable Spares, Reparable Spares, and Inventory as defined above.
3. The Inventory Control Points (ICPs) are responsible for material received and stored in each of their respective warehouse facilities and the material recorded in their logistics and financial information systems. This includes care, custody, receipt, storage, issue, disposal, location survey, location reconciliation, internal controls checks, research and resolution, supply discrepancy report initiation, safety material on ALMIS and NESSS, and investigating and assessing financial liability for loss, damage, and destruction of inventory under control of the ICPs.
4. The basic physical inventory elements include:
  - a. Conducting physical existence and completeness inventories,
  - b. Researching inventory discrepancies and causes for adjustments, and
  - c. Reconciling accountability and financial record variances (e.g., physical counts).
5. Reporting procedures exist to monitor performance measures on the effectiveness of the physical inventory control.
6. The USCG Physical Inventory Control Program complies with:
  - a. The Government Management and Reform Act (GMRA), Public Law 103-356 dated Oct 94,
  - b. The Government Performance and Results Act (GPRA), Public Law 103-62 dated Aug 93,
  - c. The Statement of Federal Financial Accounting Standards (SFFAS) #3, “Accounting for Inventory and Related Property”,
  - d. The Statement of Federal Financial Accounting Standards (SFFAS) #6, “Accounting for Plant, Property and Equipment”,
  - e. The Federal Financial Management System Requirements (FFMSR-7) Inventory Systems dated Jun 95 (includes the Chief Financial Officer (CFO) Act of 1990, and the Office of Management and Budget (OMB) Circulars A-123 and A-127), and

f. Federal Financial Management Improvement Act (FFMIA) of 1996.

B. Physical Inventory References.

1. MILSTRAP Manual, DOD 4000.25-2-M
2. MILSTRIP Manual, DOD 4000.25-1-M
3. Code of Federal Regulation, 41 CFR Chapter 101
4. DOD Supply Chain Material Management Regulation, DOD 4140.1-R
5. Shelf-Life Management Manual, DOD 4140.27-M
6. Property Management Manual, COMDTINST M4500.5 (series)
7. Physical Security and Force Protection Program, COMDTINST M5530.1 (series)
8. Information and Life Cycle Management Manual, COMDTINST M5212.12 (series)

C. Policy.

1. At a minimum, ICPs shall conduct physical inventories using auditable statistical sampling methodologies per the schedule contained in Figure 1.

TYPES	FREQUENCY/ FISCAL YEAR	PHYSICAL INVENTORY METHOD	CONFIDENCE LEVEL	TOLERABLE ERROR	ACCURACY GOAL
Reparable Spares	1 <sup>st</sup> Qtr	Random Statistical sample using Weighted Average Price (WAP) to compare WAP to documented historical costs. This does not include Sensitive, Pilferable, or Classified items.	95%	5%	95% (\$VALUE) of WAP.
Reparable Spares	3 <sup>rd</sup> Qtr	Random Statistical sample using Weighted Average Price and Net Book Value (NBV)	95%	5%	95% (\$VALUE) of WAP.
OM&S	2 <sup>nd</sup> Qtr & 4 <sup>th</sup> Qtr	Random Statistical sample	95%	5%	95% (\$VALUE) of WAP.
Remote Stock Points	Annually, 4 <sup>th</sup> Qtr	Wall to wall count (100% count?)	N/A	N/A	95% (\$VALUE) of WAP
Classified/Sensitive	Annually	100% count	N/A	N/A	100% (\$VALUE) of WAP.
Pilferable	Annually	100% count	N/A	N/A	97% (\$VALUE)
Completeness test	Quarterly	30 item count (see para 3)	N/A	N/A	95% (\$VALUE) of WAP.
End Item Association for Reparable Items	Same schedule as Reparable Spares	Sample used for Reparable Spares	Attribute Sample; 95% confidence level	5%	95% (Line Item)
Reparable or Consumable test	Same schedule as Reparable Spares	Sample used for Reparable Spares	Attribute Sample; 95% confidence level	5%	95% (Line Item)

**Figure 16-1: Physical Inventory Schedule**

**Note:** (1) Remote stock points are excluded from the quarterly random statistical sample inventory population

- (2) Refer to Chapter 10, Inventory Management, for inventory classifications and definitions.
2. The inventory of material using net book value will be conducted in conjunction with the third quarter inventory using weighted average price.
  - a. At the start of the third quarter the ICP Comptrollers will obtain the depreciation rates calculated by CG-842 during the second quarter closeout process.
  - b. Those rates will be provided to the Inventory Statistician(s) when preparations for the third quarter inventory begin.
  - c. The weighted average price of each NIIN will be reduced by the depreciation rate of the end item associated with that NIIN. In the event a NIIN is associated with multiple end items, that NIIN's weighted average price will be reduced by the average depreciation rate for its associated end items.
  - d. The depreciated NIINs make up the net book value universe.
  - e. The weighted average price and net book value inventories will follow the same processes for sampling, counting and reporting results.
3. The following applies for executing a random completeness test (floor to record).
  - a. Place all inventory locations in a file sorted by location descending order.
  - b. Select 30 locations randomly using the random number generator at [www.randomizer.org/form.htm](http://www.randomizer.org/form.htm), or randomly select the first location using the random number generator at [www.randomizer.org/form.htm](http://www.randomizer.org/form.htm) and divide the total number of locations by 30 to determine the interval of remaining locations to be inventoried. For example: If the file contains 57,000 locations, select every 1900<sup>th</sup> location after the random location is selected.
  - c. At each location record the NIIN(s) present or assigned to the location and the quantity.
  - d. Compare the NIIN(s), quantity & location combination with the record information for the location.
  - e. An error is recorded when the NIIN(s), quantity & location combination does not agree with the record. That would include too many/few of an assigned NIIN and an on hand quantity of an unassigned NIIN.
  - f. Completeness percentage is computed as follows; (1 minus the extended value of NIIN(s), [both quantity & location errors] divided by extended value of recorded inventory at sampled locations).
4. The ICP shall follow the physical inventory procedures and reporting requirements prescribed below for conducting a physical inventory, reconciling, recording, and reporting results. Results reported on the Inventory Control Effectiveness (ICE) Report shall be reported in accordance with Chapter 15.
5. External auditors shall schedule with HQ program offices (Commandant CG-41 or CG-45) and the ICPs for observation/testing of physical inventories.

6. The program office shall observe physical inventory processes and counts at ICPs every quarter to ensure conformance to policy and procedures.
7. Commandant (CG-44) shall observe physical inventory processes and counts at ICPs at least once each fiscal year to ensure conformance to policy and procedures.

D. Physical Inventory Procedures.

1. Schedule of physical inventories.
  - a. The ICPs shall provide the program office the inventory schedule for the upcoming fiscal year prior to 30 September.
  - b. The ICPs shall notify the program office of any changes to the inventory schedule as soon as they are known.
  - c. The program office shall provide the inventory schedule and any changes to the schedule to Commandant (CG-44).
2. Inventory phases. Inventories conducted by the ICPs shall include the following phases: inventory preparation, freeze, count, required research, adjustment and reporting.
3. Inventory Preparation. Conducting, at a minimum, the following pre-inventory procedures, will reduce the potential for count inaccuracies:
  - a. Perform transaction clean-up, including but not limited to frustrated receipts, error files/queues, in-transit activity
  - b. Control material movement (floor to record sampling, location checks),
  - c. Monitor shipping activity,
  - d. Address and account for controls of pre-counted material, (i.e., documentation placed on sealed box will include NSN, condition, 2 signatures and date),
  - e. Reconcile inventory records to general ledgers,
  - f. Prepare queries, and
  - g. Assign responsibility.
4. Freeze. When conducting physical inventory counts the inventory records will be locked down or the inventory item frozen until the counts have been completed. ICPs will develop processes to record manual material movement.
5. Count. The ICPs shall ensure the following:
  - a. Count sheets for the 1<sup>st</sup> and 2<sup>nd</sup> counts do not contain the quantity or total dollar value.
  - b. A minimum of two (2) persons shall be on the count team. A verifier will be assigned if warehouse personnel are utilized on count teams.
  - c. Count sheets (1<sup>st</sup> and 2<sup>nd</sup>) shall be signed and dated by all count team members.
  - d. The touch method shall be used to count inventory.

- e. Criteria for determining items that shall be exposed to weight and measure testing shall be determined by the ICPs before the count begins and shall be documented on the appropriate count sheet (s). This method can be used for multi-pack items (e.g., bolts, nuts, etc.) or bulk Items (e.g. cable, wire, pipe, etc.). The count method for these items shall be determined from weighing or measuring. The recorder shall compare the weighted or measured count to the on hand balance. If the variance is within (+/-) 5% of the on hand quantity, the count quantity shall be recorded as the on-hand quantity.
  - f. Factory sealed boxes shall not be opened. The count on the outside of the box shall be accepted.
  - g. Pre-sealed items shall not be opened under the following conditions. These boxes shall be sealed with the documentation on the outside of the box. Documentation shall consist of the date, counters names (minimum of two), condition and quantity counted. If pre-sealed boxes do not contain this information at time of count, they must be opened and counted.
  - h. Minimum requirement of one (1) count. If the 1<sup>st</sup> count matches the record, no other counts are required. If the 1<sup>st</sup> count does not match the record, a 2<sup>nd</sup> count shall be conducted. The 2<sup>nd</sup> count team shall consist of (at a minimum) two personnel, one of which was not on the 1<sup>st</sup> count team. If the 2<sup>nd</sup> count matches the record, no other counts are required. If the 2<sup>nd</sup> count still does not match the record, the count shall be recorded and the required research shall begin. When a 3<sup>rd</sup> count is conducted, it is considered part of the reconciliation phase and not part of the count phase. Third counts **are not** blind counts and are signed and dated by counters/research personnel.
  - i. Separation of duties shall exist for count and recording personnel.
6. Required Research. The following minimum research applies in accordance with minimum research requirements for potential or actual physical inventory adjustments listed in Figure 16-2 and explained in the following paragraphs.
- a. Post Count Validation. Conduct a reconciliation count (third count). The count sheet may list the quantity and dollar value. If the post count quantity matches the Inventory Management (IM) stock record quantity, then no other research is required and the count is correct. The physical count is considered correct. If a variance still exists, continue research in accordance with the minimum research requirements listed in Figure 16-2.
  - b. Pre-Adjustment Research. Post to the IM stock record any outstanding material receipts and issues pending in the system queue. If a receipt or issue pending in the system queue corrects the imbalance between the IM record and physical count then the physical inventory count of the item is considered correct. No other research is required. However, if a variance still exists after posting all outstanding material receipts and issues from the system queue; proceed with research in accordance with Figure 16-2.
  - c. Causative Research. Review inventory history files, un-posted receipts, pending shipments, in-transit and frustrated material, and temporary and special project

locations for missing items. Post inventory transactions (e.g., from receipts or issues) discovered during the research process that were previously incorrectly or not properly posted, contributing to the record imbalance. Likewise post any previous inventory adjustments that were missing to correct the record imbalance. If posting these transactions corrects the variance then no other research is required. If the variance still exists after review and/or research, post an inventory adjustment transaction. Record the adjustment on the ICE report under Number of Adjustments Posted.

**Note:** A reduction of the volume of inventory adjustments can only be achieved by conducting specified degrees of research before posting the adjustment transaction. However, in no case shall adjustments be processed against items without performing required research in accordance with Figure 16-2.

Condition of Variance	Required Research		
	Post Count	Pre-Adjustment	Causative
	Validation	Research	Research
< \$500*	Yes	No	No
≥ \$500 but < \$5000	Yes	Yes	No
≥ \$5000	Yes	Yes	Yes
Suspected Fraud, Waste, or Abuse	Yes	Yes	Yes

**Figure 16-2: Minimum Research Requirements for Potential or Actual Physical Inventory Adjustments**

\*Causative research shall be conducted on all variances of classified and sensitive items, regardless of the dollar value of the item or extended dollar value of adjustment. Causative research shall be conducted on all variances of pilferable items with an extended dollar value greater than \$100.

7. Adjustment. All inventory adjustments are the responsibility of the ICP Commanding Officer. However, approval authority is required in accordance with Figure 16-3.



Dollar Value Adjustments per line item of OE materiel		Approval Authority
<i>From</i>	<i>To</i>	<i>Gains/Losses</i>
\$0	\$499,999	ICP Commanding Officer or designate
\$500,000	\$999,999	Program Office: Commandant (CG-45) or Commandant (CG-41)
\$1,000,000	OVER	Commandant (CG-4d) via Commandant (CG-44)

**Figure 16-3: Approval Authority for Adjustments**

**Note:**

- 1) All losses of controlled inventory items must be reviewed by the commanding officer or their designated representative. Supply fund inventory is not included in figure 16-3. ICPs shall follow approval authorities as prescribed above. ICPs may modify approval authorities for a more restrictive approval policy internal to the ICP.
- 2) Research and adjustment is not required for low dollar items (less than \$50 unit cost) with high on hand quantities (greater than 100) when the extended dollar value of the on hand quantity is within 5% of the book extended dollar value and less than \$500. The book value shall be assumed correct. This does not apply to items coded as classified, sensitive, or pilferable.

8. Reporting.

- a. Physical inventories shall be completed within 20 days of the start, unless a written extension has been granted by Commandant (CG-44). Figure 16-4 summarizes the reporting schedule.
- b. Within five (5) business days after completion of post counts, the ICP shall report (electronically) to the program offices the preliminary results of both the completeness and existence tests. The report will include variances after the post count.
  - Preliminary completeness test results will include: number of locations counted, extended value of sample, number of locations with variances after the post count, extended value of locations with variances after the post count, preliminary dollar value accuracy.
  - Preliminary existence test results will include: Line items sampled, extended value of sample, number of items with variances after the post count, extended value of items with variances after the post count, preliminary line item and dollar value accuracy.
  - When reporting preliminary net book value inventory results include from the net book value universe: Line items sampled, extended value of sample, number of items with variances after the post count, extended value of items with variances after the post count, preliminary line item and dollar value accuracy.

- c. The ICP Commanding Officer shall sign and certify the final results of the physical inventory. The results shall be forwarded to the program office within 20 days of the initiation of the inventory.
- Final Completeness Test Results include: number of locations counted, extended value of sample, number of locations with variances after the post count, extended value of locations with variances after the post count, and dollar value accuracy.
  - Final existence test results will include: Total line items in universe, extended value of universe, number of line items in sample, extended value of sample, number of line item adjustments, extended value of line item adjustments, percent of total line items sampled, percent of extended value sampled, dollar value accuracy.
  - When reporting preliminary net book value inventory results include from the net book value universe: Line items sampled, extended value of sample, number of items with variances after the post count, extended value of items with variances after the post count, preliminary line item and dollar value accuracy.
- d. The ICP will notify the program office within 35 days of the start of the sample count if the inventory results are not within the accuracy goals set forth in Figure 16-1 and will identify plans for corrective action. The ICP shall perform root cause analysis of all variances to identify human, procedural or system errors, which adversely affect inventory accuracy.

<b>Action:</b>	<b>Due No Later Than:</b>	<b>Originator:</b>	<b>Recipient:</b>
Preliminary Results	Day 5*	ICP	Program Office
Final Results	Day 20	ICP	Program Office
Corrective Action Plan (CAP), if applicable	Day 35	ICP	Program Office
Program Office Review of Final Results	Day 35	Program Office	CG-44/CG-84
Program Office Review of CAP, if applicable	Day 50	Program Office	CG-44

**Figure 16-4: Physical Inventory Reporting Timeline**

\*Due within 5 Business days of completion of post count.

9. Documentation Standards. The following physical inventory documentation shall be maintained at the ICPs in an audit ready state for three (3) fiscal years plus the current fiscal year in accordance with the Information and Life Cycle Management Manual referenced in paragraph B.8. The documentation shall include the following:
- a. Copy of general ledger trial balance summary sheet or system query before snapping a sample count (printed at the time the statistical sample population is extracted).

- b. Comparison of universe to trial balance summary and reconciliation of differences (universe should match general ledgers within 1%).
- c. Data file containing exclusions (e.g., frozen assets).
- d. Copy of ICP Stat Sample procedures/checklist if changed from previous quarter (signed and dated).
- e. Confidence limits of Stratified Random Sample for the Variables Summary using Expected Values.
- f. Strata Boundaries & Size
- g. Observed sample with mean and standard deviation calculation on the observed listing.
- h. Copy of observed variances sheet dated and signed with NIIN, record quantity, quantity in location(s), nomenclature, unit price and total dollar value after post count.
- i. Statistical sample consolidated list with NIIN, location, nomenclature and unit price. Copy of stat sample count sheets, dated and signed by all team counters with NIIN, quantity, location, nomenclature and unit price.
- j. Copy of random numbers generated for completeness test, list of locations associated with random numbers and completeness test count sheet(s).
- k. If requested, causative research (copy of adjustments, screen prints and reports, transaction analysis worksheets (signed and dated)).
- l. Confidence limits on Stratified Random Sample for Variables Summary with Adjustments.
- m. Surveys, if required w/approved signature and date.

E. HQ Program Review.

1. Within 5 days of receiving the preliminary physical inventory report from the ICP, the program office shall review and reply electronically with the results of their review. The program office shall forward a copy of the preliminary physical inventory report with results of their review to Commandant (CG-44).
2. Within 15 days of receiving the final physical inventory report from the ICP, the program office shall review and reply electronically with the results of their review. Program offices shall forward a copy of the final physical inventory report with results of their review to Commandant (CG-44).
3. The program office will review and approval ICP Corrective Action Plans. Program Offices will provide resources and additional guidance when appropriate. Program offices shall forward a copy of the ICP to Commandant (CG-44).